

REDIRECTING FARM POLICY

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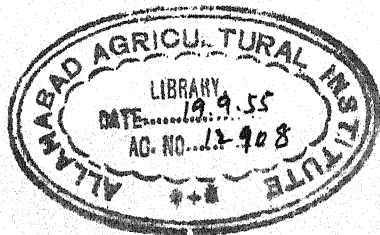
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PREFACE

We have been engaged in a great tug of war over parity prices. It has been a struggle over false issues. It has done much harm by diverting our attention from the basic issue, namely, the task of managing our food supply, its production by farmers and its distribution among consumers. The simple fact is that it is immaterial whether out of this pulling and hauling we settle on 90 percent, 100 percent, or 110 percent of parity, or on some other figure. One is as unworkable and as irrelevant to the task of economizing our food as is another.

Before we can make any headway, however, in getting back to the policy decisions that matter, we must understand what prices are for; how prices function in the management of farm resources, incomes, and the distribution of food. Once we see prices in this role and understand how they work, which is not difficult and on which there is substantial agreement, the parity price controversy will fade away. We will see it for what it is, namely, a distracting episode.

The purpose of this book is simply to get the interested public, farm leaders, and others back to a consideration of real and significant policy issues. In the last two sections we venture to suggest a series of positive proposals which are important in redirecting agricultural policy.

This book, like other studies put out by the economists at Ames, is not the product of a person working in isolation. Quite the contrary, this book has benefited in many ways from the criticisms of others in the group. Ideas have been

shared freely. For some years the need for separating the problem of managing farm resources from the problem of obtaining a better distribution of income has been a part of the Ames atmosphere, in seminars and discussions generally. It is hard to say just when certain notions have taken form. Professor G. S. Shepherd has been approaching the issue which I deal with under "Forward Prices" as part of the problem of controlling the supplies of farm products, while D. Gale Johnson has been working on the theoretical difficulties involved in forward prices as part of his doctoral dissertation. Professors A. G. Hart and Gerhard Tintner have directed attention to the uncertainty problem.

The first draft of this manuscript was reviewed critically by Professors W. W. Wilcox, Margaret G. Reid, Rainer Schickele, A. C. Bunce, A. G. Hart, and W. H. Nicholls of Iowa State College; by D. Gale Johnson, temporarily with OPA; and by Herman Southworth of Agricultural Marketing Administration of the USDA.

I have also profited from the insight and judgment of farm leaders who see these issues in the larger political setting in which national policy is formulated. Francis Johnson, President; Allan Kline, Vice-President; and Roger Fleming, Research Director of the Iowa Farm Bureau; Ralph Smith, Master of the Iowa Grange; James Patton, President of the National Farmers Union; and Donald Murphy, Editor of *Wallaces' Farmer*—each took pains to comment on the limitations of the exposition and analysis as it appeared in my first draft. To each of these individuals I am indebted. It should be taken for granted, however, that none except the author is responsible for the product as it stands.

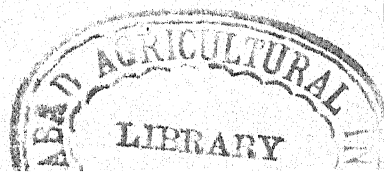
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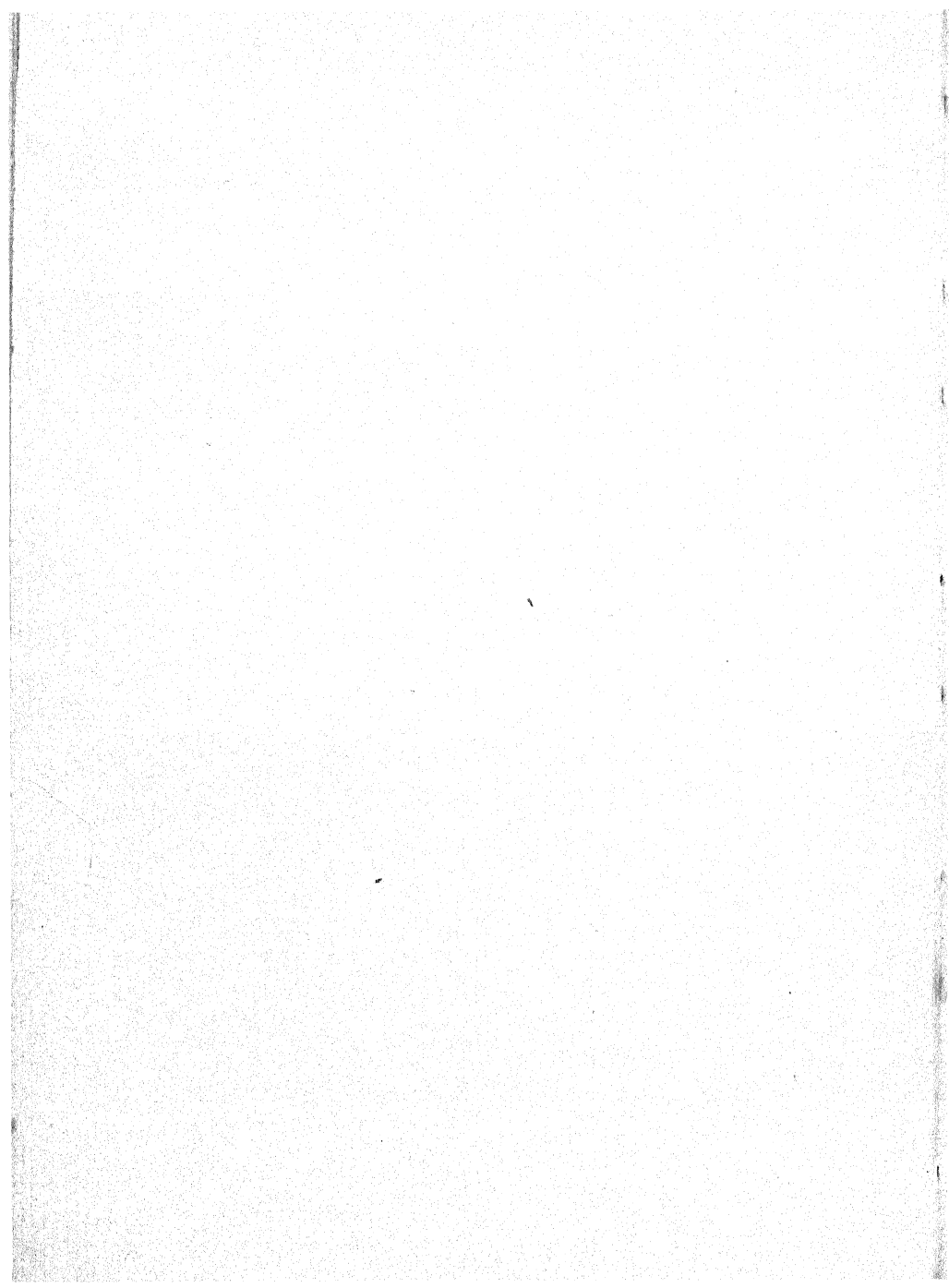
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REDIRECTING FARM POLICY





One. TOWARDS AN ADMINISTERED FARM ECONOMY

Agriculture was once the classic example of free enterprise, privately and competitively managed. It is now subject to many types of government control.

During the past ten years there was created the powerful Agricultural Adjustment Administration, with its spectacular programs to curtail farm output; the Commodity Credit Corporation, with its crop loans and ever-normal granary storage programs; the Soil Conservation Service, designed to stop the wasting of our soil resources; the Farm Security Administration, created to help low-income families in agriculture. There is crop insurance, rural electrification, disposal of surplus commodities, and market agreements. The work of the older Farm Credit Administration was greatly expanded. Finally, with the war, farm production and marketing have been tremendously influenced by the program of lend-lease purchases.

All of this represents a vast extension of the sphere of government. These new programs lie largely outside the traditional policy fields on which students of economics have in the past focused chief attention—such spheres as fiscal and monetary policy and international trade. Hence there is no extensive literature to rely upon for basic guid-

ance and appraisal. The new agricultural policy is comparatively uncharted.

Are there basic economic directives which interrelate the great variety of programs now under way? Their heterogeneity does not evidence it. But these programs were launched under emergency conditions that precluded the careful study which should have gone into their formulation. And even had there been more time, there was inadequate previous experience. Cross purposes and lack of coordination were to be expected.

It is our contention here that comprehensive economic directives do exist in terms of which these varied programs can be appraised and coordinated. By now past trials and errors have provided the experience necessary for seeking out such basic principles and applying them. The failures and successes serve also to emphasize the importance of undertaking such a search and attempting to bring order out of the present confusion.

The usual starting point for an analysis of agricultural policy is to examine the agricultural problems that the government is trying to solve. They are legion, and their sources diverse—misuse of land and out-of-date institutions; changes in growth and movement of population; depletion of resources; introduction of new techniques.

Another and more fruitful approach in giving breadth and insight, however, is to examine agriculture as part of the total economy and to study the economic difficulties that arise within this larger relationship. It is this route which we intend to follow. It will lead us back to the specific agricultural problems, but with added understanding of the basic economic elements to be considered in dealing with them.

Two. A PART OF A LARGER WHOLE

Modern society has three fundamental interests in agriculture,

1. How farm resources are used;
2. How farm families live; and
3. How the food supply is distributed.

These interests are present both in peace and war. They are always focused much more sharply during war. The stake all of us have in the performances of agriculture—also of labor, steel, railroads, etc.—is more immediate and vital when the exigencies of war are upon us. Yet it is not in war alone but, while less urgent, also when peace prevails that the agricultural economy is vested with the public interest.

First, we have a stake in agricultural production. We want enough food and fiber and we want it to be of the type most needed. We want to be sure that the farm resources are being used to their best advantage. In wartime this concern about farm production becomes acute simply because much more food is required. Civilian consumption of food jumps because people have more money to spend and because they work harder. Food is needed for the armed forces—a young man, as a civilian, may eat 150

pounds of meat; as a soldier he needs twice that much. More farm products must be sent to our allies and stock piles must be accumulated to meet the unforeseeable exigencies of war. At the same time, it becomes harder to produce or to import food. Shipments from outside sources are either curtailed or cut off altogether. Both the armed forces and the war industries draw heavily upon the man power in agriculture. Farm machinery and fertilizer are rationed, and transportation becomes increasingly harder to obtain.

Second, we have a stake in how farm people live; this depends upon the size and distribution of the farm income and upon the way in which farm families use it. We all have a social stake in the rising generation, in public health, and in citizenship. Our building blocks are education, nutritious foods, adequate clothing, housing, and medical services.

Third, the distribution of the food supply between poor and rich, between civilians and armed forces and among the United Nations during the war is of primary importance. Normally, we depend upon prices to allocate the available food supply. As the spending power of consumers mounts, however, it is not enough simply to shift agricultural production into high gear and let the output go to the highest bidder. The amount of money that consumers have to spend on food is not a satisfactory index of their needs for food. The war is teaching us that other criteria must be employed.

During war we also want safeguards against inflation. What farm families do with their incomes has a direct bearing on the problem. Larger farm incomes during the last war resulted in a land boom that left in its wake farm foreclosures and years of financial distress. Will this occur again as farm incomes climb?

Our main point is simply this: Do the present agricultural programs succeed in guiding and directing (a) the use of resources, and (b) the size, distribution, and use of incomes of farm people, and (c) the distribution of the food supply among consumers in such a way as to serve the general interest best? It is this basic question which underlies the inquiry that follows.

The war has already helped clarify several of these issues. It has been instrumental in revealing quite clearly both the merits and limitations of some of the farm programs. The war, in this sense, is a kind of testing ground, for it is placing the public machinery designed to serve agriculture under a severe strain, quickly exposing weaknesses, as well as strength, which would not become apparent for years under peacetime conditions.



Three. PRICES AS GOALS OR AS DIRECTIVES

Recent events have called attention to the outstanding weakness of the present farm and food programs, namely, the type of price policy under which the Department of Agriculture and the Office of Price Administration are administered. This shortcoming has shown up in the management of the food supply both on the production and consumption side and in what is being done to improve the distribution of income among farm families.

In one sense, the Department of Agriculture has had not a comprehensive policy but a number of specific programs, each designed to do a particular task—crop control, storage, commodity loans, soil conservation, surplus disposal, crop insurance, and others.

In another sense, all of these programs have been tied to parity prices. Thus it might be said that parity prices have provided the Department with an over-all policy. In this, the aim has been to control supplies, use loans and storages and other devices to attain parity prices. Thus, parity prices have been looked upon as price goals, as ends, to be attained. Consequently, prices have not been used as a technique for guiding and directing farm production except as the resulting production favored parity prices.

It is now quite apparent that parity prices are inappropriate guides for managing agricultural resources.

Why hasn't this shortcoming in farm policy been recognized and corrected? It is indeed significant that the elements of a price policy have received little or no consideration in the discussions of farm policy. The emphasis has fallen on the specific programs—the crop control features of AAA; the granary loans of CCC; the low-income help of FSA; the food stamp plan, school lunches, and other disposal schemes of what was AMA; the erosion control and soil practices of SCS; etc.—and not on the function of prices. The same thing has happened in other fields. It appears to be true of the whole price policy of government; OPA and the legislation under which it operates also view prices or a kind of price change as goals, not as economic directives.

As a consequence, we have come to a crisis in agricultural policy centering on prices.

Before it is possible to forge a new policy, many old attitudes and beliefs about the function of prices will have to be re-examined and changed. Prices must be seen and employed as economic directives and not as goals. Until this step is taken, there can be no straightforward analysis of the elements of a price policy for agriculture.

The price mechanism is a powerful instrument with which to manage the farm economy and the distribution of the food supply. The mistake that has been made is that, as the government took a hand in the management of the production and distribution of foods, it attempted to do this by a whole series of particularized programs, not realizing that a master price policy was necessary to coordinate the total effort. Furthermore, there has been a lack of appreciation of the positive contribution of prices when employed as an active instrument of control.



Most of the confusion and misunderstanding that have arisen among farmers, farm leaders, and congressmen, and among the administrative personnel of the government, about price policy can be traced back to differences in their views as to what prices are expected to accomplish. Broadly speaking, there are two views: (1) those who look upon prices as goals, namely, as ends to be achieved, and (2) those who see prices as one of the means for guiding and directing economic activity. Let us explore both the merits and limitations of these views.

PRICES AS ACTIVE DIRECTIVES

Prices have a function, and that function is to direct and regulate economic processes. This approach places prices in the category of means by which things are directed. That prices can direct is richly documented by our experiences. Applied to agriculture it means that the price mechanism is a technique for managing the food supply both in order to get the most out of our resources and to distribute it to consumers. It takes one set of prices to induce farmers to use their resources most effectively. It takes another set of prices to distribute the food among consumers most wisely. Not that the management of either production or consumption in this sense can be accomplished wholly by systems of relative prices; far from that, for prices are but one of the means of doing these two jobs. They are, however, by all odds the most basic and far-reaching administrative technique yet devised for directing and coordinating both the production and distribution of the food supply. Whether the farm economy is administered privately or largely by public agencies, our past experience emphatically demands that the price mechanism be employed. Farm production involves the decisions of literally millions of entrepreneurs, each confronted with a different set of resources, and con-

sumption involves the decisions of even more millions of consumers with widely different needs, tastes, and purchasing power. These decisions and actions can be effectively coordinated only through prices.

The function of prices can be put into bold relief by focusing upon the notion sometimes expressed that prices are passive indicators rather than active directives. This passive approach is negative in its outlook, because it rests on the belief that farm prices as well as other prices are made by fundamental economic forces over which man and society have little or no control. It sees prices as merely reflecting the results of what has already happened; thus to use prices to manage food supplies is like attempting to change the barometric pressure by fixing the barometer. This passive view which sees prices as indicators is best expressed in the popular phrase, "supply and demand make prices." What the layman loses sight of when he uses this phrase is the fact that neither supply nor demand is independent of price; the nature of the dependency is left out.

Back of this passive view there also usually lurks the belief that economic processes function and stay in balance automatically if left to themselves, or, to put it another way, that the economic system is essentially self-regulating. This idea of the self-regulating propensity of the economy is frequently fostered by those who have selfish interest in maintaining the particular market mechanism that happens to prevail. When this occurs, the slogan "supply and demand make prices" is turned into propaganda to delay necessary reorganization of the price mechanism.

There are several other types of objections to the approach that it is the function of prices to direct economic activity which may be anticipated at this point. Many people are still mindful of the situation during the depression of the early 'thirties when the price mechanism

had in fact little directive power. Changes in the differences among prices were largely overshadowed by the decline in prices. This certainly was true within agriculture. The corn-hog ratio turned somewhat more favorable, but this was of no particular consequence. For instance, hog prices dropped from \$9.00 to \$3.00 and corn from 70 to 20 cents a bushel, in Iowa between 1930 and 1932. Changes in relative prices under such circumstances lose their power to direct either consumption or production. What happens is that once the flow of income to families starts dropping and prices generally start falling rapidly, the price mechanism loses much of its ability to coordinate economic processes.

Similarly, during inflation, when resources are virtually all employed and when most prices are rising rapidly, the mechanism of relative prices does not function satisfactorily. The flow of income to families then increases more rapidly than the output of goods available to consumers, and as this occurs an inflation potential is developed which greatly lessens the directive powers of the price mechanism. This simply means that changes in relative prices become secondary while the general upward drift of all prices dominates the decisions of producers and consumers. This objection to the way prices function, growing out of our experiences with deflation and inflation, does suggest that the price mechanism is most effective when there is no radical change in aggregate incomes—the period 1935-1939, for example.

Another objection to prices as active economic directives is voiced frequently by those who are concerned about the problem of income distribution; they object to the market price machinery because it fails to distribute incomes to families in accordance with general welfare. This shortcoming of the price mechanism in distributing personal incomes has led many persons to contend that it is antisocial in its effect and therefore should be replaced by other administra-

tive machinery. This point of view is closely akin to the "fair" price argument.

This objection to prices as they affect distribution of income is born of the failure to distinguish between the problem of managing resources and the problem of improving the distribution of personal incomes in modern society. These are two distinct though interrelated categories of problems. Solving the first does not solve the second. The techniques for managing resources are not always appropriate or adequate for correcting maladjustments in income. The point is that, until the problem of resource management and the problem of improving the distribution of income are separated and seen as two distinct issues, no rational economic solution can be forthcoming.

PRICES AS GOALS

The idea that prices are a kind of goal has dominated farm legislation. Parity prices are the result. The same view is present in the legislation and administration of OPA. What it comes down to in practice is that both in OPA and the USDA particular prices have been designated by law as objectives to be attained.

This tendency to place prices in the position of ends is the most serious stumbling block to any progress toward a more rational economic policy, not only in agriculture but in other fields as well. The management of supplies is made increasingly difficult. War, however, drives home the lesson that it isn't prices that we want—what matters is whether we manage to get as much food, steel, aircraft, tanks, etc., out of our resources as is possible. Prices are simply administrative machinery for doing this task.

While it is easy to demonstrate that prices are not appropriate as goals, it is much more difficult to get at the reasons why people generally are disposed to believe the contrary.

There are several roots which have supported the growth of the parity price approach.

First, and probably foremost, has been the long struggle of farm people and their leaders for what they have called "equality for agriculture." As this ideal was translated into legislation, after the farm group had won its political battle, the notion of equality for agriculture came to mean parity. To start with, parity was a distant objective made up of political, social, and economic values considered essential to an "equality for agriculture." As time went on, however, there unfolded in farm legislation the notion of parity formulated as an economic concept in terms of prices.

The over-all idea that it is desirable to maintain a certain basic parity among economic groups has general appeal and is valid when properly understood. This is still what many farmers and others have in mind when they speak of the *parity principle*. They have in mind social, political, and economic status and not specific prices related to any given date. Accordingly, one must be sure when an individual speaks of parity whether or not he has in mind these more general interrelationships which go to make up the over-all values for which people strive or whether the concept is being used in its narrower, more technical sense, a price index of the type that has been written into farm legislation.

A second support for the idea of parity price has come out of the particular way in which farm prices behave relative to other prices during a depression. It is well known that, when a depression hits, farm prices have fallen faster and dropped to much lower levels relatively than wages, salaries, prices of services, and for that matter prices of nearly all manufactured goods. This places the farmer in a peculiarly vulnerable position because his costs remain high while his selling prices drop.

When farmers experience the kind of price situation that

prevailed in 1932, 1933, and into 1934, it is easy to see why they should seek protection and, if possible, devise measures which will keep a depression from distorting their price at some future date. To keep farm and non-farm prices at least somewhat in line with each other is their objective. To give expression to this desire, they have turned to parity prices, for this has meant to them a way of keeping their selling prices from dropping faster than other prices.

A third factor in the development of the parity price concept has been the need for some measuring rod to get at the performances of the public agencies serving agriculture. No one can deny the fact that there has arisen the need of appraisal; someone has to evaluate—in the first instance presumably Congress—how well or how poorly a given agency has performed its task. This need for establishing criteria of performance is now of primary importance. In many ways it is the key to whether or not it is possible to make an administered economy actually work.

To appraise the results of what each of the several public agencies in agriculture do, it is necessary to have agreement on the nature of the goals to be achieved and on tests for determining the extent to which the goals are attained. The importance of appraisal has received all too little attention, especially from students of agriculture. The task of finding and establishing appropriate criteria for measuring the accomplishments of farm programs has been left altogether to the lay leaders in agriculture and to Congress. They have turned to parity price as a device for accomplishing this task. Parity price has appealed to them for a number of reasons. It appeared to them as being concrete and practical, specific and precise, as having economic content and being sufficiently simple to be understood.

Still another support for parity price has come from the strong conviction, which many people have, that each family

should earn enough to provide for itself an adequate income. This is the substance of the idea of a "just" or "fair" price. It has long had general social sanction and is in fact deeply embedded in our standards of ethical values. A fair price means simply that the rate of payments which a farmer, laborer, or capitalist receives for his services and the use of his property is sufficiently high to provide each with an adequate income. To the individual the notion of an adequate income is usually highly subjective, with its expectations rooted mainly in past standards of living. However, to a community or a society in general the idea of an adequate income may be objectively ascertained in terms of nutrition, health, education, and other criteria of social welfare.

In much of the discussion and support for parity price there is the belief that farmers must receive a fair price; that is, a price for the products they sell which will give them an adequate income, meaning at least enough income to maintain the standard of living to which they have become accustomed.

Looked at in this way, parity prices are a special case of the much larger class of so-called "fair prices." This view is rooted in our social philosophy. It is based on the belief that those who labor, those who have industrial plants, and those who farm should receive a rate of return for their work and investments that is sufficiently high to "earn" for them an adequate income. No one would contend that a fair price or its subclass, parity price, thus formulated is intended to facilitate the most economical use of agricultural resources.

This aspect of parity prices, however, is of general significance in determining policies that affect, on the one hand, the management of agricultural resources and, on the other, what we do about the size, distribution, and use of

farm family income. It will be necessary, therefore, to examine the difficulties it presents in more detail later in the discussion, when the elements of a price policy for production and for consumption are considered.

Is it any wonder that the idea of a parity price has become so firmly rooted and so formidable a stumbling block to more rational price policy? From this brief survey we see that parity price has had the support (a) of those who seek equality for agriculture; (b) of those who are apprehensive about the depression squeeze on farm prices; (c) of those who are trying to find a yardstick to measure the performance of public agencies in agriculture; and, finally, (d) of those, a very large group indeed, who believe that fair prices provide families with adequate incomes.

RESOURCE MANAGEMENT TIED TO PARITY PRICES

Any set of prices representing some past period is always out of date when applied to current production. This simply means that, no matter whether 1910-1914, 1919-1929, 1924-1929, 1934-1939, or any other period is employed in calculating parity, some prices will be too high and others too low. The production effects of such prices are obvious.

Rye, wheat, horses, and mules are examples of items that are greatly overvalued by parity as of June 1942.¹

	<i>Parity price, dollars</i>	<i>Dollar value as resources (estimated)</i>	<i>Overvalued, percent</i>
Horses (per head)	208.00	80.00	62
Mules (per head)	234.00	100.00	57
Rye (per bushel)	1.09	0.50	54
Wheat (per bushel)	1.34	0.85	37

¹ For an analysis of specific farm prices and parity see my *Farm Prices for Food Production*, a pamphlet in the "Wartime Farm and Food Policy" series, Iowa State College Press, Ames, Iowa.

Products from which meats, oils, and fats are made are examples of farm commodities that are currently undervalued by parity.

	<i>Parity price, dollars</i>	<i>Dollar value as resources (estimated)</i>	<i>Undervalued, percent</i>
Cottonseed (per ton)	34.00	45.00	32
Beef Cattle (per 100 pounds)	8.25	10.75	30
Hogs (per 100 pounds)	11.00	13.50	23

Is it any wonder that the USDA and OPA are constantly getting themselves into bad price situations? Being tied to a price formula of the parity type, they must resort to subsidies, storage, and other devices to offset the production effects of the prices which they force too low or keep too high. Specifically, the USDA because it is tied to parity in its wheat programs has been forced to "overprice" wheat, with the result that more and more wheat piles up, overtaxing storage facilities and keeping much wheat land from producing other crops that are required more urgently. Meanwhile, OPA holds the price of some fats and oils down and not enough resources are used in producing oil-bearing crops and animal fats unless a subsidy is provided. Some prices are too high and others too low for best production.

In substance, parity prices are backward-looking. They represent the dead hand of the past. Tying parity to 1910-1914 makes it obsolete by thirty years. It is not possible to force agriculture back into a set of price relationships that existed three decades ago. If this were done, it would put our economy into a strait jacket, the consequences of which would be to force resources into uses many of which are wholly undesirable. It would greatly lower the efficiency of our farm economy.

If parity price is obsolete, why didn't it get agriculture into serious difficulties prior to this? Why is it that the event of war has made parity prices appear suddenly unmanageable? On the surface one might suppose that the higher prices occasioned by the war should have made the parity less difficult to handle.

The parity price formula did not create serious problems during the early years of the New Deal chiefly because it was used mainly as a broad, general directive to improve economic conditions within agriculture. Congress gave the Department of Agriculture considerable latitude in applying the formula. The 1938 Agricultural Adjustment Act specified loan rates ranging from 53 to 75 percent of parity. This range for administrative action forestalled most difficulties. Unfortunately, however, during the spring of 1941 Congress insisted on a much more rigorous interpretation, as evidenced in the mandatory farm commodity loans of 85 percent of parity. Then came the 90 percent loans and the 110 percent ceilings. This change, curtailing the range for administrative discretion, came at the very time when the economic effects of the war were beginning to make themselves felt and in doing so were making past price relationships increasingly unrealistic.

War is highly dynamic. It is, in fact, violent in the upheavals it brings, for it changes radically the values placed upon the goods and services that the economy produces. It has been the war, therefore, that has exposed the weaknesses of parity prices. It has done this more convincingly than have all the analyses which economists have put forth.

Our conclusion is easily put: Parity prices, whether tied to 1910-1914 or to a more recent date, whether or not they are refined to take account of regional differentials and of the quality differences of a commodity, much as these

refinements help, are not suitable goals for farm policy simply because it is the function of prices to guide and direct economic activity. To accomplish that purpose, prices must be kept in the position of management machinery, always forward-looking.

There remains, however, the question: What about those who for one reason or another have supported the idea of parity price? The issues they have been concerned about are real and important and accordingly deserve further comment.

What about those who associate the parity idea with that of "equality for agriculture?" They will have to differentiate between the broad concept and the much narrower price thing. The *parity principle* should stand as a basic over-all approach to social, political, and economic forces where conflicts and community of interests prevail and where it is essential to keep a balance. This broad view, however, should not be confused either with parity prices or with parity income. The latter concept is also inappropriate for guiding the management of farm production, as we shall show later.

For those who are concerned about the tendency of farm prices to fluctuate much more violently than do other prices, a phenomenon which is especially disastrous to agriculture during a depression, there is no easy answer. Part of the difficulty lies in our fiscal and monetary policies. Part of it is to be found in the imperfections in competition, the fact that so much of our economy is dominated by giant firms who determine to a large extent their own price policies. Part of the problem arises out of what happens in other national economies. How to safeguard the interests of farmers who are small-scale operators, who do not have at hand the techniques to protect themselves from booms and depressions, remains in part unanswerable simply because

some of the elements are not within the control of a single national economy.

The answer to these difficulties does not lie in parity prices.

What about those who want a measuring stick with which to check performances of the USDA and OPA? Basically, on the production side, we have to go back to the principle of marginal productivity. The place to start is with production goals. Once there is agreement on what and how much should be produced, goals which reflect both the capacity of farm resources and the food required, then the task of the Department of Agriculture is straightforward and easy to define; namely, to induce farmers to use their land, labor, equipment, fertilizer, etc., to produce the amounts necessary to meet the production goals. Deficient production of some items because too much land was devoted to others would measure the shortcomings of the administering agency. Account, of course, would have to be taken of the "uncontrollable" influences of weather and related elements.

Finally, there are those who believe in a "fair" price. The issues which this view entails are reserved for a later section when we consider the role of "supplementary income" in modern society.

Four. RESOURCES AND INCOMES

A great obstacle to redirecting farm policy is the failure to distinguish between managing resources and managing income. Most of our farm programs have been designed on the belief that these two problems are essentially one and the same. This view is evident in nearly every piece of farm legislation.

In AAA the idea has been to curtail the acreage of corn, cotton, wheat, and of other so-called basic crops of which farmers were producing too much. To induce farmers to cut acreages, benefit payments are paid. These payments go largely to the farmers with the bigger incomes. Thus, quite aside from whether or not farm land is put to a better use because of the efforts of AAA, the distribution of income among farm families has been worsened. For example, in 1935-1936 in the heart of the corn belt, farmers with money income below \$1,000 received about \$100 from AAA, while farmers with incomes of \$3,000 or more were paid over \$400. In the cotton belt the dispersion has been even greater. White operators in Mississippi with incomes of \$1,000 or less received about \$55 from AAA, whereas those with incomes of \$3,000 or better averaged well over \$1,000 in cash from AAA. The effect of the commodity loans upon the

distribution of incomes has been similar. When the loan rates have been above market prices, farmers with the most land and crops have gained much more from the loans than have farmers with low or inadequate incomes.

Why do we persist in lumping together the resource problem and the income problem in policy making? The main reason is that we have failed to understand the interplay between resources and incomes. We have assumed connections between them that do not exist. We have assumed that remedying the maladjustments in the use of farm resources would necessarily improve farm incomes. And, on the other hand, we have assumed that when we took steps which improved farm incomes, these would necessarily result in a better use of resources. Neither of these two assumptions squares with the facts.

We shall also show that price policies which are appropriate for the management of agricultural resources should not be tied to income goals.

There is room for much improvement in the way our agricultural resources are used. In the South, we have kept too much land, fertilizer, and labor growing cotton and not enough producing peanuts, feed crops, and livestock. Wheat also has claimed too many acres. Many farmers are using outworn and outmoded equipment, poor seed, and not enough fertilizer because they lack capital, do not know the merits of better practices, or cannot do a better job because of the tenure situation in which they find themselves. Nor is agriculture peculiar in having many resources poorly employed. The same thing is true in labor, transportation, manufacturing, retailing, and the professional services. In one sense, with the rapid changes in process new maladjustments in production are inescapable. What we should seek is an organization and management that are efficient in making the necessary readjustments.



There also is room for much improvement in the way farm income is distributed and in the way in which farm people live. About half of our farm people are situated in the South. Most of these receive wholly inadequate incomes. In 1941, a very prosperous year indeed, over half of the farm families in the South received less than \$500 of net money income. While fewer of the farm families in other regions are as poor as in the South there still are many, especially in the once drought-ridden plains and the cut-over sections. Farmers usually have large families. Many farm children are handicapped in school, food, and medical care. These inadequacies are closely associated with the small incomes of their parents and communities. Also in this, agriculture is not alone in having a poor distribution and some unwise use of income. The problem is to be found in all major divisions of our society. Certainly many non-farm families are the recipients of inadequate incomes.

Let us first see how resources and income are connected.

In a competitive society the incomes which families receive in the form of interest, rent, and wages tend to be in accordance with their economic productivity. Thus the amount of income depends upon the amount of productive property the family possesses plus the value of its labor. Families which have the kind of services and property that produce a lot receive large incomes. Obviously, talented persons who render services for which society is willing to pay a high price—for instance, some actors, writers, managers—and who in addition have acquired or inherited much valuable, productive property get large incomes. In contrast, a head of a household who, because of the limitations of his talents, training, health, and general environment, can do only work which has a low economic value and who has inherited or acquired no productive property, gets a very low income, often too little to support his family.

In a strictly self-sufficient, Robinson Crusoe, household economy the resources and income problems would blend and become essentially one. Production and consumption would be integrated by the head of the household. But most farms are not self-contained in our modern, highly interdependent exchange economy. A society in which property, talent, and training were distributed equally enough among all families to permit those with the least of these assets to earn an income sufficiently large to support their families at some minimum standard would also resolve most of the income problem and leave that of production. Such a society, however, is a far cry from what now prevails. Income-producing property and talents are not distributed in a way that would minimize the nature and scope of the income problem.

Thus we are confronted with both resource and income maladjustments. They usually call for quite different treatment. The guiding hand for managing resources is the principle of marginal productivity. To improve the distribution of family incomes we turn to social welfare criteria for guidance. It is not enough to see and do only one of these tasks. Gains on the production side are desirable and all to the good. But they alone do not assure us a maximum of general welfare. A more equitable distribution of income is also a gain, but not a corrective for many of the maladjustments in farm production. There are some measures, as we shall show directly, that contribute both ways, and these should be used to their fullest advantage. In the main, however, two types of programs are required.

INCOME EFFECTS OF BETTER PRODUCTION

One of the false notions about the connection between farm output and revenue is that a better use of farm resources necessarily improves farm income. It may do so and it may not. For instance, many improvements in production

come from advances in farm technology. Technical progress in farming has been rapid. Let us briefly outline the income effects of new farm techniques.

Generally speaking, farmers who first adopt a new technique usually increase their income because they reduce their cost, while the additional output they produce has little or no effect on price. It is this margin between cost and price during this stage which acts as a strong inducement to adopt a new technique. As more farmers take it on, this margin is likely to decline and even vanish. During this stage, there frequently is a period when the price of the product declines more than the reduction in cost occasioned by the new technology. This period is prolonged by the slowness with which agricultural resources are transferred when an unbalance arises between price and cost. Over the long pull, when a new balance has been attained, the income effects depend primarily upon the elasticity of demand and substitution. If the technique is of the hybrid seed corn variety, the main effect probably is to reduce the scarcity of corn land and accordingly the relative value of such land; consequently, the income of families who have capital invested in such property is thereby reduced. When the technique is chiefly labor-saving, it is likely to cheapen the value of that particular type of labor.

Society gains from the introduction of a new technique by farmers because the benefits are general and consumers' terms of exchange improve. In this gain, farm families also participate as consumers, both from the advances made in their own technologies and from those adopted by other producers. Nevertheless, the introduction of a particular technique such as a tractor, combine, or hybrid seed may have, probably usually has, an adverse incidence on the income of farm families during the later stages of the resource adjustments it occasions.

The income effects of soil conservation are similar to those of farm technology. When public funds are used to reduce erosion and soil depletion, costs of production are likely to be lowered. But when most farmers take advantage of these public investments to conserve soil the lower costs are soon reflected in lower food prices simply because of the competitive character of agriculture.

To take still another example, when the demand for a farm product changes, we have the following income effects: An expansion in the demand gives the farm family producing the product a *windfall*, especially when the family owns the land and farm equipment; conversely, a contraction in the demand causes the family to suffer *losses*.

Much of the low-income problem in agriculture is tied up with cotton and wheat and is caused in part by declines in demand. Shifting some land and farm labor out of cotton and wheat into other uses results in real gains to society, but it does not necessarily restore farm incomes. Many farm families are likely to be forced out of these areas by the necessary production adjustment.

To review: New farm technology, better soil conservation practices, and land use adjustments necessitated by changes in demand each contribute to a better use of our farm resources, but we are wrong when we bank on them to increase the size of the farm income. Nor do they help the distribution of incomes.

Some programs on the resource side, however, have positive income effects. Public assistance to farm people in migrating to better economic opportunities falls into this class. Some farm people are literally stranded. They may be working hard and therefore do not appear as unemployed, but they are, nevertheless, in an economic sense "unemployed." It takes capital to migrate. New skills are usually required, and training costs money. Information is also re-

quired, and this, too, as a rule is costly. Yet migration, well directed, can do much to increase the economic productivity of many farm people by assisting them to transfer their labor to other parts of agriculture or to some non-farm occupation. Moreover, the incomes of the farm people affected are improved.

There is a great deal of capital rationing in agriculture. This simply means that many farm families do not have enough capital. To put it more precisely, additional capital in the form of machinery, fertilizer, improved seeds, livestock, and feed would yield many farmers 10, 15, or 20 percent returns while interest rates are much less. Programs which close this gap between interest rates and what additional capital would yield farmers not only give us a better use of resources, but they also help correct one of the serious income maladjustments in agriculture because capital rationing is found chiefly among the low-income farm families.

PRODUCTION EFFECTS OF BETTER INCOMES

Another belief widely held is that measures which improve farm income also bring about a better use of farm resources. How valid is this view?

One way to lift the incomes of farm people, and meet welfare criteria, is to provide all families with the minimum essentials for good health, namely, more nutritious foods, better housing, improved sanitation and medical services. These are excellent long-run investments because the ability of farm people to work is enhanced and the chance of their migrating out of areas with substandard opportunities is increased. But the results are not immediate; they are likely to be years in coming; in the main, returns show up in the next generation.

One generalization, however, to which we can tie is: All

public programs that make investments in the human agent tend to equalize incomes.

Another way to lift and equalize farm incomes is to make available to farmers the facilities for communication considered essential to our social institutions. The rural free delivery of the mails is of this type, although farmers seldom recognize it as supplementary income. Increasingly, our "all-weather" public roads are being extended into the country to serve farmers. Rural electrification is another program that belongs in this class. It is difficult, however, to see how "income" programs of this kind contribute directly to a better management of farm resources in producing the required type and volume of farm products. In some situations they may make the efforts of farm people more effective as producers; in others, however, the benefits associated with roads, rural mail carriers, and rural electric lines tend also to keep farm resources in production after they have become uneconomic because these benefits, under certain circumstances, act as a subsidy maintaining the farm when its contribution on the production side no longer warrants its operation. Studies in land use are replete with examples showing where this has happened.

Both the preceding groups of measures can be given a positive rating as techniques for supplementing farm incomes because on the one hand society, through its institutions, has something to say on how the added income is used. This it does by making the grants in the form of specific services, for instance those associated with good health and communication, which presumably are deemed necessary to social well-being. They are made available, accordingly, in such a way that they cannot easily be diverted to other uses, which is important when we consider the interest that society has in this process. On the other hand, these measures are not likely to lower general produc-

tion efficiency of the agricultural economy. On the contrary, over the long pull, they have a positive contribution to make, with few provisos.

There is, however, a group of "income" measures that are wholly negative in their production effects. All schemes designed to increase the prices of farm products by resorting to monopoly power fall into this category. This happens when a higher price is maintained than is necessary to produce the product. This is a dangerous road for any interest group to travel. It has been repeatedly pursued by business enterprises, through the use of giant corporations, cartels, patent rights, the tariff, and other devices. Labor has been induced time and again to start down this all-too-attractive highway; and in agriculture, the more strictly the interest groups are formed along commodity lines, the more likely they are to take this road. Any measures which increase the price of the services of professional people, the price of manufactured products, the wage rate of workers, the price of milk, fruit, or any other agricultural product by the use of monopoly power must be classified as strictly negative from a social point of view because of their production effects. It means that less is produced and marketed than is warranted by the availability of resources. Society as a whole loses. Real incomes accordingly are less than they would be if no elements of monopoly were present. Income measures falling in this group should be avoided.

These illustrations suffice in pointing up this conclusion: It is a mistake to proceed on the assumption that measures designed to improve farm family incomes will also guide and direct agricultural production. The task of administering production is one job; that of administering incomes is another. Although at many points the two are interrelated and complementary, they are essentially two different undertakings. They have this much in common—both are far-

reaching in their importance; both require public attention; both fall within the sphere of political economy. They differ, however, significantly in their aims, in the administrative techniques which are appropriate, and in their economic effects. The two must be separated in analysis, in policy making, and in programs and their operation. This point will be pressed one step further in considering the implications of a price policy tied to income goals.

PRICES TIED TO INCOME PARITY

There has been some support in agricultural circles for an income approach in which the price mechanism and the various farm production, marketing, and credit programs are employed to attain specific income goals. This approach has received the support of individuals in the Department of Agriculture and of some agricultural economists as a substitute for the parity price formula. Furthermore, there is some likelihood that farm leaders will go over to this view as they become convinced of the unworkability of parity price. Accordingly, it is important to examine this approach to see what are the prospects that it will provide the working rules by which the farm programs can be directed and administered.

The income goal approach has several variants. One of these is the *parity income* concept. Another is expressed in the phrase, "agricultural share of the national income." The procedure and argument for this scheme falls into three stages, each of which must be examined separately. First, society is classified into two or more major categories, either farm and non-farm or, as has been done more recently, into agriculture, labor, and capital. A comparison is then made of the per capita or per family incomes, treating each of these categories as a homogeneous group. When this calculation has been made, it shows that the average per capita

and per family income in the farm or agricultural category is lower than in the others.

The second stage involves the setting up of a formula covering income relationships as of some past period, such as 1910-1914, when the relative incomes of farm people as a whole appeared to have been somewhat more favorable compared either to the non-farm category or to labor and capital. The assumption is that incomes would be better distributed if this former relative income structure were re-established. It makes a past set of income relationships a goal to be attained.

The third and final stage in this approach is to advocate using the farm price mechanism, for example, the price of corn, wheat, cotton, and of other farm products, to increase the income of the producers concerned to re-establish the relative position of their income in line with that which prevailed during the base period.

Before discussing the limitations of this approach, it should be noted that income parity is based on a historical period which in discussions thus far has usually been 1910-1914. It might, however, be based on a more recent period, say 1935-1939 or any other, without changing the principle of the approach. In this respect, the procedure is the same as that employed in calculating price parity, using income data instead of price data. Another aspect is that income parity may be calculated on various geographical bases as far as agriculture is concerned. For example, a single formula may be used for all of agriculture; or one may be established for each major agricultural region. This breakdown may be taken further and a formula established for each type of farming area, and presumably it could be carried to an individual farm basis. This suggests two variables in computation; namely, that of the base period and that of the geographical area included. These features,

however, pertain to the mechanics of the concept, while our primary concern in this critical analysis is with the principle that underlies the entire approach.

This idea of tying farm prices to pre-established income goals rests on three critical assumptions: (1) that a comparison between occupational categories, each of which is exceedingly heterogeneous, has significance in analyzing incomes; (2) that the criteria for improving the distribution of incomes are to be found in the income structure of some past period; (3) that the means for improving farm incomes is the price mechanism of farm products. The first of these assumptions involves the use or misuse of statistical techniques. The second raises the question: What are the criteria for ascertaining the adequacy of incomes? The third presents the issue whether or not prices on the production side are appropriate means for effecting a better distribution of incomes. Let us examine each in turn.

Whenever the differences within a class are greater than those between classes thus constituted, statistical averages may lose their significance, and this is precisely the case in income comparisons that bundle together such over-all categories as farm and non-farm people. Because each class is made up of families differing widely in the range of their incomes, the relatively small difference between the two classes loses its significance. It simply means that a wrong type of classification is being employed. What is important is the number and the proportion of families in particular income classes, regardless of whether they are in agriculture, industrial labor, or some other occupation, and not what the average income of the prosperous and the depressed families added together happens to be.

A few figures from *Consumer Incomes in the United States* will illustrate our point. These data are for 1935-1936. Take first the non-relief families with incomes below \$250.

For the United States as a whole, 2.8 percent of all families were thus classified in contrast to 3.8 percent of the farm families. Even this should suggest that these very low-income families are not peculiar to agriculture. The regional figures, however, reveal that farm families are not necessarily even more frequent in this class than are others.

*Percent of families with
income below \$250*

New England	
Large cities	1.6
Farm	1.2
North Central	
Small cities	2.7
Farm	2.2
Southern	
Small cities	5.9
Middle-sized cities	5.8
Non-farm rural	5.0
Farm	3.4

We can also use non-relief families with incomes below \$500 to show how incomes overlap and interrelate. For the nation 10.7 percent of all families received incomes below

*Percent of families with
income below \$500*

New England	
Large cities	6.4
Farm	6.4
North Central	
Small cities	7.6
Farm	7.7
Non-farm rural	8.8
Southern	
Small cities	18.3
Middle-sized cities	17.0
Non-farm rural	18.9
Farm	24.1

\$500, whereas 17.7 percent of the farm families were this low. Again, observe what happens when regional data are examined using the same regional groups.

It might be inferred that the objection to over-all categories is overcome by dividing farm people into regional or commodity groups or, even better, on a type of farming area basis. This refinement in no way lessens the limitations of data thus classified. For example, when 50,000 farmers are classified as appearing within a hog-corn-beef type of farming area, among this group of farm families there exists a wide range in incomes. These variations arise, first, from the differences in health, talent, and training, as these contribute to the farmers' ability to manage and to the capacity of the members of the family to work. Second, differences in income arise from the amount of productive property that families have acquired or inherited. One family may be starting at the bottom of the agricultural ladder with little or no capital (actually there would be some whose net worth would be a minus), and other families may have 320 or more acres of land with well-improved buildings, drainage, and fences and with all the necessary machinery and livestock free of debt; meaning, often \$25,000 to \$40,000 of capital. To add the incomes of farmers having as wide a range in income as these, ascertain an average, and conclude from this that the income the families are receiving is either adequate or inadequate is meaningless indeed.

The import of all this simply is that income comparisons of this type are highly misleading because of their statistical composition. This is not to argue that there are not many low-income families in agriculture. The contrary is true. The objection is simply to these procedures of identifying low-income farm families.

Take next the step of selecting a base period. There is no more justification for going back to some historical in-

come structure in improving the distribution of incomes than there is in going back to some past set of price relationships and using these as price goals. The criteria for improving income and its distribution are inherent in considerations of general welfare. This concerns welfare economics. The task is to determine the claims of social justice as these reflect and contribute to the general interest. It confronts us with the whole matter of values in modern society. There is, it would appear, sufficient agreement to make some of the criteria sufficiently objective to serve policy making. This can be done in terms of standards of nutrition, housing, health, education, and other related benefits. Social welfare thus conceived is positive and forward-looking and not a compound made up of the values inherent in the income structure of some historical period, such as 1910-1914.

There is one further critical comment on this approach in which the aim is to re-establish the income relationships that prevailed during some past period. The issue is best focused by a question: What justification is there for returning to and freezing the relative poverty and prosperity in which people found themselves in some former period? The income, for example, of many farm people producing cotton and many other products has been wholly inadequate regardless of the base period one selects. Certainly, the general welfare is not served by programs seeking to establish and maintain income relationships of that type. Conversely, there are groups of farmers, whether one takes them by commodities or by type of farming areas, who have been the recipients of unusual windfalls. Again, we ask: Why should it be deemed essential to the general welfare to perpetuate these highly favorable returns simply because during a particular base period a group of producers happened to enjoy exceedingly high incomes?

The main point, however, should not be lost; namely, that the only rational basis for testing the adequacy of the income which a farm family receives is in terms of social welfare. Unless this is done, the process becomes irrational and arbitrary.

Finally, there is the third assumption: that the way to increase the size of the farm income and improve its distribution is by controlling the prices of farm products in order to get the desired farm income. It is at this point that farm prices become tied to specific income goals. The aim is not that of getting the required production but that of getting a certain farm income. They are two quite different things. There are at least three serious objections to this procedure.

In the first place, raising the price of a farm product does not necessarily increase farm incomes. The demand for many farm products is not inelastic. This means simply that jumping a price 10 percent would cause consumers to cut their purchases 10 percent or more. There is also the fact that, while consumers are not likely to cut purchases and to shift to other products quickly, given a little time they adjust their buying habits in ways which further increase the elasticity of the demand. For many farm products, when we consider both the changes in cost and revenue, a somewhat lower price and higher output would actually increase farm incomes. The range for which this holds is fairly narrow, however, and a big crop usually exceeds the mark.

In the second place, raising the price of farm products does not improve the distribution of income among farm families. Even when a higher price actually increases the income of the producers concerned, it does not reduce the range among incomes. As a rule, a higher price is likely to help those with low incomes less than it does farmers already enjoying large returns. Experience shows that an advance in the price of cotton, hogs, or almost any farm product

tends to increase income to those farmers receiving the largest returns much more than it does to those at the other end of the income scale.

The third objection is by all odds the fundamental one; namely, that any attempt to tie the price mechanism of farm products to parity income goals would destroy the usefulness of prices in managing agricultural resources. To follow the dictates of such income goals would distort the prices of farm products and bring about a malallocation of resources. There is a wide gulf separating income and resources at this point. In the one, policy must be directed according to social welfare criteria; in the other, that of using resources, the principle of marginal productivity must prevail. This principle means, in substance, that resources should be transferred from one use to another until further shifts will not increase their productivity. There is no other rule by which society can keep house and obtain the most from its resources. In a word, it means society must, in order to pursue a rational course of action, follow the dictates of marginal productivity in all spheres of production. It is the task of the price mechanism to facilitate this objective—which prices cannot do when they are tied to specific income goals.

The sole purpose of this section has been to show why it is necessary to separate the resource problem from the income problem. While they overlap, are interrelated, and are often complementary to each other, in policy making they must be kept separate because the principles that govern the selection of programs and of administrative techniques are wholly different. On the production side, economic knowledge appears to give a conclusive answer. Rational behavior requires that resources be used according to the principle of marginal productivity. The returns which

society obtains are maximized by allocating each resource in such a way that equal increments of the resource yield equal increments in value of product. This means marginal productivity. The consequences of this principle in production have been explored thoroughly in economic analysis, and there is virtually no disagreement as to its validity and application.

We cannot speak with the same certainty on the side of income distribution because less study and less experience are at hand. There is general agreement, however, that the governing principle is that of social welfare. This places it within the province of welfare economics. As yet, too little is known about programs and administrative techniques that will maximize social welfare. Usually, major institutional changes are involved when society takes steps to supplement incomes according to social welfare criteria. The fact that less experience has accumulated in no way lessens the importance of this problem in modern society. In peacetime it might well be that income distribution is of even greater significance than the economics of production which has received thus far most of the attention.

Five. POSITIVE PROPOSALS: ON THE PRODUCTION SIDE

Our analysis up to this point has appeared somewhat negative since it has stressed chiefly the basic limitations of the present farm policy. This has been necessary in order to provide background and appraisal. It is now possible, however, to proceed to the other side of the ledger and outline certain positive proposals for redirecting farm policy. In doing this, we shall first consider policy appropriate to farm production, leaving the field of income for the next section.

It is well to pull together at this point the separate threads of the preceding discussions which bear upon the elements of a price policy for agricultural production.

- One.* We have been moving toward an administered farm economy with public agencies in control. The war has further accelerated this trend, and agriculture is likely to require much public attention during the postwar years.
- Two.* It is the general interest of society which must be served in the use to which agricultural resources are put. This interest is best served by allocating each resource according to the principle of marginal productivity.

Three. The farm price mechanism is probably the most effective over-all administrative device available to public agencies for bringing about the type and volume of agricultural production which society needs and which farm resources are capable of producing.

Four. Farm prices are a means for guiding and directing agricultural production. They are economic directives; they should be employed to induce farmers to produce those products and services which best serve the needs of society. To accomplish this purpose, farm prices must be employed as positive instruments of control. They must be forward-looking; they must anticipate both the changes in the needs of society and the changes that are occurring in resources. It is not possible to employ prices to accomplish these purposes if they are tied (a) to a parity price calculated in terms of some past set of price relationships, or (b) to a parity income based on the income structure of some past period.

The nature of the positive proposals to which this summary points is self-evident. Above all else, on the production side the farm price mechanism should be employed by the Department of Agriculture to guide and direct agricultural production.

To do this task, it will not suffice to reinstate a system of market prices of the type that prevailed, let us say, prior to 1930. A highly decentralized farm price system administered, in the main, by private agencies has many serious shortcomings.

Two major steps are required to bring about a more efficient system of farm prices, steps which are now possible with the technical staff and the administrative machinery

at the disposal of the Department of Agriculture. In authorizing this procedure it will be necessary for Congress, however, to orient the farm program along the lines of the Steagall Amendment without tying it to parity price. The two required steps are:

1. Production goals, and
2. Forward prices.

PRODUCTION GOALS

The first of these is already being done by the Department of Agriculture. In placing the farm program on a war footing, the Secretary of Agriculture has established the administrative machinery for determining production goals. Back of this step, however, lies a long history going back to the time when the "Outlook" programs were first initiated by the Department. The purposes of the Outlook were to bring together all of the supply and demand information for each farm commodity, analyze it and interpret it in terms of the type of production changes that were most likely, to advise farmers of the nature of the Outlook, and to indicate to them the type of production adjustments that would bring the best results.

Much rich experience for the formulation of production goals has been gained from the preparation of the Outlook. It led to intensive studies of the nature of the demand for farm products, including that of consumers at home and market outlets abroad. It also gave rise to research into the response of farmers to changes in price, and this in turn led to various types of studies of the resources used in agricultural production. Consequently, the staff of the Department of Agriculture has acquired much local, national, and international information necessary to formulate production goals. Let us see what is meant by a production goal.

A production goal should satisfy the following conditions. (a) It should be that volume of production which best represents what our food and fiber requirements are and what agriculture is capable of producing. (b) It should be determined in sufficient time to enable the Department of Agriculture to announce prices to induce the necessary production. (c) It should be revised whenever our requirements have changed and when it is possible for farmers to alter their production plans.

It is plain that no group of farmers, no set of buyers and sellers in any organized market, have at their disposal the expert information and staff to formulate production goals as accurately as can the Department of Agriculture with its vast fund of data, highly trained technical experts, and administrative machinery. Consequently, it would appear that it is possible to develop within the Department a headquarters staff whose task it would be to formulate production goals which reflect the capacity of agricultural resources to produce and the needs of society better than can any other machinery with which we have any experience.

There are, however, some difficulties. There is always the danger of special interests, both outside and within the Department of Agriculture, making themselves felt. When they do this, it might not only bend but even thwart the staff making the estimates. The influence of outside groups should not be underrated. The force of groups within is such that safeguards are warranted. For example, if one of the agencies within the Department has a particular interest in the production goals being larger or smaller than the situation warrants, it may have sufficient influence to alter the results. With the present action programs administered by the Department, it is hard to imagine a time when one or more of the larger agencies would not feel considerable concern about the production goals that

were established. Take, for instance, an agency which has accumulated large stocks; in order to ensure the disappearance of the stocks, it would welcome a production goal smaller than the true situation might warrant. Or again, when an administrative agency is motivated by the theory that agriculture is served best by curtailing production, it is likely to be adverse to production goals that accurately reflect requirements and might well use its influence to have them modified downward.

There is still another difficulty growing out of the disposition of individuals responsible for formulating production goals to defend them at a later period, even though the changes which have transpired fully justify an upward or downward revision. What happens is that people acquire a "vested interest" in the production goals they have formulated. Consequently, past estimates are put in the best possible light, and it is easy when doing this to fail to give an accurate portrayal of a new supply and demand situation.

It is well to recognize that in determining requirements for food and for other farm products the estimates of the Department should be closely scrutinized from the general public point of view. These estimates of requirements should reflect as accurately as possible the general interest.

It is in these requirement figures and the production goals that we have real, meaningful criteria for evaluating the performances of the Department of Agriculture. Congress and the various interest groups have tried to employ parity prices for this purpose. They are not suitable, as we have pointed out. Production goals, however, might well serve this purpose. There is no reason why Congress should not be advised and possibly approve each year the production goals that best reflect both the amount which agriculture is capable of producing and the requirements of society. This having been done, the Department should be author-

ized to use its administrative machinery to attain the production goals as established. These goals would provide a very specific, precise, and quantitative set of criteria against which to check the successes and failures of the Department.

The proposal of having an expert personnel charged with the responsibility of formulating periodically production goals for agriculture has much in its favor. This procedure in all probability will give results which, taken as a whole, will be much superior to what takes place when private individuals make estimates, usually acting on fragmentary information and all too often on hunches.

FORWARD PRICES

The second step in employing the farm price mechanism to allocate farm resources is to establish a system of forward prices. Thus far, we have had little experience with this procedure. It has been tried in the case of soybeans with satisfactory results.

The idea of a forward price is new,¹ and accordingly some pains must be taken at this point to understand what it means. A forward price should meet the following specifications.

- One.* It should be that price which is necessary to induce farmers to produce enough to meet the production goal.
- Two.* It should be announced sufficiently far in advance to enable farmers to make their production plans.
- Three.* It should be established to cover a sufficiently long time so that farmers could carry out their production plans with some certainty.
- Four.* It should be made sufficiently precise in terms of

¹ See the section on "Positive Proposals" in my paper, "Economic Effects of Agricultural Programs," in *American Economic Review*, Proceedings, vol. 30, Feb. 1941.

the grade and quality of the commodity and the time and place at which the price would be in effect so that every farmer could interpret the price in terms of his operations.²

Forward prices are a gigantic futures market operated to coordinate and direct agricultural production.

Forward prices are not goals but a part of the necessary machinery for doing a first-class job in agricultural production.

Forward prices shift to the Department of Agriculture the task (a) of formulating production requirements, and (b) of assuming some of the risk and uncertainty now borne by farmers.

When the national government undertakes the task of administering farm prices with one eye on food requirements and the other on farm capacities, it must decide what policy to follow with regard to price changes. How often should farm prices be changed? Is it necessary to have them change every day? once a week? monthly? Or is it desirable, under present circumstances, to fix farm prices for the duration of the war?

Price administrators have essentially three alternatives in this matter, namely:

1. Let farm prices stay highly flexible and subject to change without notice;
2. Fix farm prices for the duration of the war or even for a longer period; and
3. Establish farm prices far enough into the future to cover the next production period and change them at the time a new production period starts.

The tug of war in the political arena tends to focus on

² This list of specifications is essentially the same as that given by D. Gale Johnson and the author in Memo No. 5, "Elements of a Price Policy for Agriculture," Iowa Agricultural Experiment Station, Ames, Iowa, May 15, 1942.

the first and second of these choices. Tradition is on the side of letting farm prices stay exceedingly flexible. Administrators are prone to prefer this position because it forestalls decisions on their part, and it does not tie their hands. In the other camp, we find the interest groups in agriculture inclined to bargain for as long a period as possible, not only for the duration of the war but for fixed price guarantees for several years after the war. There has been a growing disposition on the part of political leaders to promise fixed prices that extend into the postwar period. It is our contention that neither of these two approaches is satisfactory. The highly flexible farm prices under which agriculture is operated are not consistent with maximum production. It is a wasteful and obsolete price system because of the nature of the firm that predominates in agriculture, namely, the small family-type farm. To swing to the opposite pole, however, and fix prices for agricultural products for several years in advance introduces a rigidity which will be exceedingly costly in terms of the misuse of agricultural resources that is likely to result. Not only will society be burdened by this procedure, but farmers are also likely to lose in the process.

How frequently farm prices should be changed depends primarily upon the nature of the changes that occur from time to time in food needs and upon the production effects of farm prices. The production consequences of changes in farm prices may be classified into those which induce farmers to alter their production plans and those which give rise to economic uncertainty. What we want in practice is as much of the first and as little of the second as possible. The objective, therefore, can be put very simply. It is two-fold; namely, to *maximize* those price changes which are necessary to keep farm production in line with food needs and with other changes in the economy and to *minimize*

those price changes which contribute to economic uncertainty in farming.

Is it possible, however, to separate in practice these two types of production effects, one of which is essentially positive and the other negative? Is price uncertainty a necessary by-product of the changes in farm prices which must be made in order to guide and direct farm production; must we continue to accept the bad with the good? From the fragmentary evidence now available, it appears that these two types of production effects which flow from changes in farm prices can be separated, since some price changes do not give rise to uncertainty, while other price changes have that attribute. A price change which is expected and which is known sufficiently in advance of the time that production plans are made does not necessarily give rise to uncertainty. On the other hand, changes in prices which are not anticipated, which simply happen and which follow no discernible pattern, breed uncertainty.

A first approximation to a solution separating these two types of production effects lies in synchronizing the date when production plans are made by farmers and the date when prices are changed. By having these two dates coincide, it is possible to minimize price uncertainty and to maximize the effectiveness of price changes in directing farm production.

To illustrate this approach, take soybeans. Soybeans are an annual crop, which means that production plans are made anew each year. Thus the general level of soybean prices should be changed once a year. This change should come at the time farmers make their plans for producing the next crop. The fact that soybean prices are to be changed again the following year, at or somewhat prior to planting time, does not necessarily introduce price uncertainty in farming. We have, therefore, as example a change in price without

price uncertainty. The key to the whole matter is one of timing, namely, in having the changes in farm prices coincide with the periodicity of farm production, the latter be-

ans of farmers.

ep further. The price sonally to compensate, There is no reason why change within the year odification of the gen- d for the year. Such a e to price uncertainty. n in advance, farmers e crop with full knowl- isonal change of price. r soybeans, or for any roduction period does vell reflect the cost ele- n agricultural produc- hanges in demand that therefore can be antici-

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them in the past, have ore frequently, and the been greater than any How has this system of ractice? What are the y who have referred to

this flexibility in farm prices as a shining example of how prices should function. According to this view, the day-to-day and even hour-to-hour changes in farm prices are highly desirable in contrast to the less flexible prices that charac-

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Schultz, Theodore W
Redirecting farm policy.
Macmillan, c1943.
75 p.
N.Y.



terize most other sectors of the economy. Back of this view lies the assumption that constantly changing prices have desirable production effects. It has never occurred to those who proceed on this assumption that frequently changing prices also may lead to waste and economic maladjustments.

Let us put the problem as follows. What can the farmer do, confronted as he is by prices that are constantly subject to change? Since there are, in fact, no means by which he can determine the direction or the magnitude of the price changes which are likely to occur, what choices are open to him? Presumably, he might do two things: (a) decide to disregard the fluctuations in prices and simply go on producing, following the crop rotation and livestock plan which he has inherited or hit upon; or (b) he might decide to weave flexibility into his farm operations in order to be able to shift quickly the use of his resources and in this way at least try to take advantage of price changes as they occur. Both of these procedures involve a cost, and it may be a high cost indeed, both to society and to farm people.

By pursuing the first of these two alternatives, the farmer decides for all practical purposes to forget about price fluctuations in his management plans and operations. In practice it would mean a kind of traditionalism in farming which might be characterized by its insensitiveness to price changes. There is, in fact, a good deal of this attitude in agriculture. Farmers who take this view go on doing what they did a decade or even a generation ago, presumably because they believe or have learned from experience that to try to guess what the market is likely to do is useless and a waste of time and to attempt to change production plans every time farm prices change gets them nowhere. It is not difficult to see what this means to the national economy. Changes in relative prices lose their capacity to coordinate and direct farm production as this attitude be-

comes established. Farmers who have become insensitive to price changes and who accordingly choose to operate along some traditional line obviously fail to respond to the changing needs of society. Food requirements are dynamic in their nature; for example, we may need more fluid milk and less butter, more peanuts and less cotton, more wheat for feed and less for flour. Farm prices may be altered to reflect these new food needs, but to the extent that farmers develop an immunity to changes in farm prices they are not induced to make the necessary transfer in the use of farm resources. Consequently, because of the lack of dependability which has characterized farm prices, farmers continue to produce as of old, regardless of new needs and regardless of changes in farm prices that reflect these needs. As this kind of reaction becomes established in farming, there is bound to arise a lag in production adjustments, a gap between what is produced and what is needed. Consumers lose by not getting the type and volume of food they want most urgently; farmers lose by growing products which are less valuable than those which their farms are capable of producing. To the extent, therefore, that farmers confronted with constantly fluctuating prices become insensitive to price changes we reduce, if not destroy, the capacity of relative prices to guide and direct farm production.

The farmer may, however, decide to take the other road. He may seek to introduce flexibility into his farm organization which would permit him to change his production plans and operations quickly and thus attempt to take advantage of the changes in farm prices as they occur. To illustrate, inasmuch as the relationship of the price of corn to that of hogs changes frequently, the farmer might decide when hogs are cheap relative to corn to build corn cribs and store the crop rather than feed it to hogs. By building enough

corn cribs he can manage the corn side of the problem, especially if corn loans are made available to him to finance the operation and provide for current income at the same time. When hogs are dear relative to corn this farmer might decide to build extra hog barns, fences, and feed lots to make it possible to feed more hogs and thus convert more corn into livestock, not only his current crop but also the corn which he has accumulated. The flexibility which this farmer has acquired in his production operations by building extra corn cribs and extra hog barns, fences, and feed lots is one way of responding and dealing with constantly changing farm prices. It entails, however, much excess plant capacity which adds to the cost. Nor are these the only extra costs involved in this type of production flexibility.

At this point, we must distinguish between price changes which are necessary for dynamic reasons and those which are unnecessary. When farmers develop flexibility in production to handle unnecessary price changes, there is an economic loss, a wasteful use of resources which can be avoided. Resources which are used to build corn cribs, livestock fences, feed lots, and barns that are only used part of the time and have been acquired by farmers in response to unnecessary price changes are a measure of this loss.

While we have stressed the role of flexibility in production and its implication to cost, it should be noted also that the usual family-type farm is technically too small to introduce this kind of flexibility. In the main, the resources at the command of farm families are too few to permit them to build the extra corn cribs and the extra hog barns, the type of equipment that is necessary in order to have operational flexibility to adjust to unexpected changes in farm prices. This means that, even though farmers attempt to organize their farms with a view to obtaining flexibility and thus involve themselves in higher costs which presumably, in the

long run, are reflected to consumers in higher prices, technically it is not possible for farmers to pursue this road very far. Thus, the road which involves production flexibility with its higher cost is but a partial solution to the problem of farm prices subject to change without notice.

FIXING FARM PRICES FOR LONG PERIODS AHEAD

The consequences of fixing farm prices for the duration of the war or even for a longer period, one extending several years into the postwar era, are probably more apparent to price administrators, farm leaders, and the public generally than are the effects of highly flexible farm prices already discussed. Supposing farm prices were fixed for the next three years, what would happen? Plainly, farmers would be the recipients of an unprecedented bit of price certainty. It is hard to foresee how much of a boom this would be to farm production. No doubt, it would result in a substantial increase in farm output, even with the growing scarcity of man power in agriculture. It would act as a powerful inducement to forego flexibility considerations and use farm resources thus released to expand current output. Specifically, farmers would be less disposed to keep corn under seal but instead would feed it to livestock and sell it as animal products. To put this feature of fixed prices in another way: It is quite probable that a farm price guaranteed for two, three, or more years and on which the farmer accordingly could bank in making his production plans would have a very considerable capacity to bring about additional production, probably as great as prices one-sixth to one-fourth higher of the uncertain type which has prevailed, say, during 1941 and 1942. In this, we have a clue to the "cost" inherent in price uncertainty in farming. It is our contention, however, that virtually all of these costs attributable to price uncertainty can be eliminated by a sys-

tem of forward prices subject to change at the beginning of each production period and, further, that such a price policy would also avoid the losses that are likely to occur when farm prices are fixed for long periods. These losses are of several kinds. They rise from the fact that anticipated supplies and demands do, in fact, change as a consequence of dynamic forces. We know that food requirements, for example, are likely to change appreciably while the war lasts and that they are certainly going to be different after the war. Many aspects of these changes are not predictable. If they were, we could weave them into the price structure and to that extent there would be no problem in fixing prices for the duration and longer.

As these unpredictable changes occur—for instance, in food requirements—it is essential to translate them into production goals and necessary prices to obtain that production if we are to maximize farm output. To go on producing, say in 1944 and 1945, on the basis of production goals and farm prices that satisfied 1943 conditions, disregarding changes in food needs in the interval, is to deny ourselves as a nation the best use of our farm resources. It would mean that we would not produce, for example, the types or volumes of food which we would then need most urgently. It is quite probable that it will be necessary a year hence to curtail the output of some farm products in order to make possible a larger production of others. For example, it might be necessary to cut the production of butter sharply in order to have more milk for fluid and dry uses. It might be necessary to expand the output of the oil-producing crops, such as soybeans and peanuts, at the expense of oats, and cotton. Developments of this type in food needs would call for shifts in the use of farm resources. Under such circumstances, to continue with a structure of farm prices which was appropriate this year would result in real

losses to society. It would mean waste, a misuse of farm land, labor, and equipment. It might be argued that some of this waste could be avoided by supplementing the old farm prices with subsidies in order to induce farmers to make the shifts called for by the new food requirements. But why resort to subsidies? Why not change farm prices, some up and some down, in such a way and at such a time as not to breed price uncertainty, but to ensure the very shifts in production which are in line with the new food needs?

FORWARD PRICES FOR A PRODUCTION PERIOD

The choice, however, is not between leaving farm prices to fluctuate from day to day or fixing them for several years ahead. Price policy should steer its course between these two extremes. The course to be followed should be charted in terms of production periods. Specifically, each farm price should be established for one production period ahead and no longer. This presents two points which are quite technical in nature. One of these is that of selecting the period for which the price is operative in order to have it coincide with the time span of the production plans of farmers. Another is that of making transitions from one production period to another. Both of these steps, it would appear, however, are basically technical details in view of the larger objective and the probable merits of this price technique. The advantages are several.

In the first place, it would permit each farmer to plant the crops and feed the livestock which he can produce most cheaply, which does not happen when acreage allotments or marketing quotas are employed to direct and control farm production. These latter techniques always increase the costs of many farmers. The forward price would give the farmer a dependable selling price for the next production period.

He would have a definite price on which to base his plans. He would then proceed to produce that combination of crops and animal products in which he has the greatest advantage in view of the resources at his command. His thought and his energy would go into farming and not into trying to outguess the market.

In the second place, a forward price would transfer from the farmer to the Department of Agriculture part of the burden of price uncertainty which arises during the time span when the farmer is in the process of producing his crops or livestock. As we have indicated, much of the real inefficiency and waste in the use of farm land, labor, and capital grows out of the uncertainties that confront the farmer as he plans and carries through his production operations. To eliminate these uncertainties is likely to cut farming costs appreciably.

What are the implications of transferring to the Department of Agriculture the burden of bearing price uncertainties? There are several angles. Some of the price uncertainties would disappear in the process. To the extent that the Department can formulate more accurate price expectation than farmers are able to do, mistakes in farm production would be reduced. An excellent example of this is the case of hogs late in 1940. Changes in prospective demand made it apparent that this country was headed for a shortage in pork. Farmers, however, were making their breeding plans for the coming year on the basis of the \$6 which was then the prevailing price for hogs and not upon the information that more pork would be required in the near future. The price of hogs was so low that it called for further liquidation in spite of the fact that the prospective demand situation was such that more rather than fewer hogs should be produced. Looking ahead at that time only three to six months, a \$9 price for hogs was fully justified,

and this would have been sufficient to have brought about a notable expansion both in breeding and feeding of hogs. As it turned out, even a \$9 forward price would have been too low in view of the supplies of pork that were required during 1941-1942.

Another aspect of what happens when price uncertainty is transferred to the Department is that some of these uncertainties take on the characteristics of risk when they are handled by a single agency, simply because the Department in contrast to a farmer deals with large numbers both geographically and over time. Accordingly, certain errors tend to cancel out. In addition, a central agency like the Department has machinery for correcting its position by measures that an individual farmer usually cannot employ. There are three ways in which this can be done.

1. The Department could build up stock piles to act as a cushion to offset some types of miscalculations. When the output was too small, part of the stock pile might be used; conversely, part of an unexpectedly large crop could be earmarked and added to the stock pile. Storage machinery of this kind is especially suitable to products that have a low rate of deterioration, products which are fairly durable like wheat, corn, and other cereals, canned meats, and certain other processed foods.

2. The Department might correct for new developments by the use of equalization funds, one for each of the various clusters of farm commodities. When the demand exceeded expectations, the fund would be replenished; and when the demand fell below expected levels, the fund would be drawn upon. Conversely, for unexpected changes in supply. More specifically, when the demand for a product increased unexpectedly and the price rose higher than the forward price, an assessment would be made on each unit of the product sold to equate the difference between the forward price and

the higher price at which the product is most efficiently distributed through marketing and retail channels. The revenue thus obtained would go into the equalization fund. When the opposite situation arose, namely, when the demand receded unexpectedly and prices dropped below the forward price, the product would be sold at a price lower than the forward price, and the difference would be taken from the equalization fund and paid to farmers in order to give them the announced forward price.

3. The Department might also correct its position when the amount produced or marketed exceeded expectations by disposing of some of the product through channels other than the usual market outlets. This technique is especially applicable to perishable products. In using this approach, what happens is that secondary and somewhat unrelated demands for the product are tapped. This procedure, however, could also be used to broaden the market generally; when thus employed, it usually would involve subsidies. Its merits in this sphere depend upon its contributions to the general welfare in terms of diets and better health of the people who benefit from these disposal schemes, of which the school lunches and the food stamp plan are excellent examples.

A forward price of the type herein advanced will probably reduce measurably the cost of agricultural production because of increased efficiency in farming. One example: with hog prices fluctuating from \$12 to \$6 every few years there is much waste, for farmers during one period overextend their production facilities and use too much feed and, in another, let their feed lots stand idle. During the transition periods as prices drop farmers liquidate their hogs, selling them young, unfinished, and rough; and as prices rise, farmers feed their hogs to weights far beyond those which give the best product from the point of view of consumers.

This is a wasteful use of corn and other feeds, a process which has characterized much of the livestock economy in past decades as it has been directed by market prices. No one would claim for a moment that consumers favor these periodic swings in livestock production, with the amount of meat available to them changing sharply every few years.

A measure of the reduction in cost associated with forward prices may be inferred from the present meat situation. Under the current ¹ ceilings imposed by OPA on the wholesale prices of pork, live hogs have been selling at or near the \$15 mark in Chicago. To many farmers this figure does not appear unreasonably high with hog prices going up and down as they continue to do. Most farmers would readily exchange, say, a \$13.00 price for hogs on which they could depend with certainty as they make their breeding plans for next year, for the unpredictable \$15 price which might occur under OPA ceilings. In this instance, a reduction in price of nearly one-seventh might be effected by bringing certainty into the selling price of hogs. Moreover, most farmers would consider the lower price on which they could depend a much better proposition, and it in turn would not only assure some further expansion in production and hence more meat, but also lower pork prices.

FORWARD PRICES DURING WAR

Forward prices have two positive features in administering the farm economy during war. The added certainty would act as a powerful incentive to increase production, and this property of the forward price should be used. The extraordinary response of farmers in soybeans in 1942 illustrates how an assured forward price works. Last spring, prior to planting, the Department announced a specific price for 1942 soybeans. The price appeared low relative

¹ During part of August, September, and the early part of October 1942.

to corn, the crop with which soybeans compete most directly. Yet the resulting increase in soybeans was nothing short of phenomenal, with the crop harvested for beans jumping from 5.8 to 10.8 million acres in one year.

Still another feature of the forward price technique is its usefulness in combating certain price distortions caused by inflation. At present, with the rapid increase in family incomes and with fewer durable consumer goods available, with an inadequate rate of taxation and too few forced savings to sterilize this additional purchasing power, consumers are driving up prices of the better and scarcer foods. This new spending distorts the farm price structure and in a measure disorganizes agricultural production. Furthermore, it places a wholly unwarranted strain upon agriculture.

Because of the inadequacies in our fiscal policy, it becomes necessary to take secondary remedial measures. To combat this distortion of farm prices and the strain that it places upon agriculture, two steps are necessary. (1) Assure farmers a price for their output that will induce as large a production as is consistent with the best use of agricultural resources. This is not a price ceiling or a price floor but a forward price of the type already outlined. Such a price in most cases would be less than that which consumers with their present purchasing power are prepared to pay for farm products. (2) Keep consumer demand from upsetting the forward prices for farm products. Presumably, as in the equalization fund approach, a special assessment would accomplish this end. In effect, it would be an excise tax on particular foods to absorb the additional purchasing power, namely, the difference between the forward price and the price consumers were willing to pay for the product. This would mean that present retail price ceilings could not be maintained. Moreover, families with the most income would

get the food at a time when the distribution of food should be more nearly in line with need.

The answer lies in managing the distribution of the food supply to consumers in such a way as (a) to protect families with small incomes, and (b) to hold civilian consumption sufficiently in check to keep prices from going higher than the forward price.

ADMINISTRATIVE OBSTACLES

The difficulties in the use of the forward price technique are primarily in the political sphere.

As long as interest groups, Congress, and the Administration persist in using farm prices to obtain 1910-1914 parity prices, a system of forward prices is precluded. Nor will it work tied to any historical set of prices or to income goals of the parity income type. A price system of the type which we have outlined must be administered with one eye on maximizing the use of agricultural resources and the other on the products available to consumers. Forward prices must be based on food needs and farm capacity—more precisely, on anticipated demands and anticipated supplies.

SUPPLEMENTARY PROGRAMS

Other farm programs will have to be reshaped to complement and support a price policy of the type outlined. The establishment of farm prices, which, in the main, has been a by-product of what the various agencies in the Department of Agriculture have been doing, will have to become the master policy.

While it is not within the province of this discussion to elaborate the many changes this will call for, the direction that they will have to take may be indicated. In this, it is important to emphasize that a farm price mechanism administered as a system of forward prices will not of itself be

sufficient; in other words, supplementary programs will be required.

One of the important complementary federal agencies in agriculture is the Commodity Credit Corporation. Its storage programs are exceedingly important in adjusting for the effects of weather on farm output. To stabilize the supplies of feed which are fairly durable and of food crops which can be stored is a task which may well take even larger stock piles than we have been accustomed to, the notable exception being cotton and wheat in which we have accumulated stocks of wholly unwarranted amounts. The CCC, however, is operating under a very defective charter. The Corporation has been headed for the rock that sank the Federal Farm Board. It is hard to see how it can escape this fate as long as it is required to chart its course according to the dictates of parity prices. Mandatory farm loans at 85 or 90 percent of parity on so-called basic commodities tie the hands of the Corporation in such a way that it cannot perform its task of stabilizing supplies through appropriate storage operations. Wheat and cotton especially have been overvalued. The CCC was also getting itself into serious difficulties in corn when the war came along and turned the corn carryover into a major asset. Rising farm prices resulting from the extraordinary expansion in demands for farm products occasioned by the war have thus far saved the CCC from the consequences of the defects inherent in the organic law creating the Corporation. In defining its functions, it is necessary to start with food requirements and the resulting production goals. The nature and the scope of storage operations should be based upon food needs and farm capacities with full allowance being made for the probable variations in farm production attributable to weather. These operations cannot be performed by the Corporation as long as its loan and storage program

is tied to parity prices. It can be done, however, if loans are related to a system of forward prices necessary to induce the production called for by the production goals.¹

Another important agency which has developed functions essential to the administration of the type of price recommended in this study is the Agricultural Marketing Administration. (Recently absorbed in the new Food Distribution Administration.) The programs of the AMA are especially suitable for those products in which it is either technically impossible or too costly to build and maintain stock piles. There is, in a sense, a basic division of labor between the Commodity Credit Corporation, which deals with those farm supplies which are sufficiently durable to make it feasible and economic to engage in storage operations, and the Agricultural Marketing Administration, which also deals with the problem caused by variations in supplies but chiefly with that category of farm products which are not sufficiently durable to permit evening out these variations by storage operations. There is, however, a major difference between the two agencies in that the performances of the CCC can be tested in terms of production criteria. The AMA, however, is confronted in addition with the task of developing the elements of price policy to guide and direct consumption. It, therefore, is faced with the difficulties of integrating these two purposes. The administering of a system of equalization funds of the kind previously suggested has not been developed. It will probably require additional legislation by Congress. The technique appears to have sufficient merit to justify the petitioning of Congress

¹ Professor G. S. Shepherd has a manuscript near completion on the role of commodity loans and required prices which takes up this issue in considerable detail. He also has published two recent articles, "The Stabilization Operations of the Commodity Credit Corporation" and "Basis for Controlling Agricultural Prices," which appeared in the August and November issues of the *Journal of Farm Economics*, 1942.

for this authorization. As far as one can foresee at this juncture, equalization funds for this purpose should be employed solely for the purpose of supplementing a program of forward prices designed to guide farm production.

The contributions of the AAA to a redirected farm policy of the type here proposed are several. Should the AAA, however, persist in its efforts to control the output of certain farm products by rationing the input of farm resources, not only are its efforts likely to continue largely in vain, but its actions would entail more, rather than less, difficulty in administering a system of forward prices. On the other hand, if this agency's personnel and funds—the amount required is much less than that now expended—were employed to provide additional incentives for farmers to combine their resources more efficiently and to use better farm practices in producing those crops and livestock which society needs most, the efforts of AAA would be particularly important in supplementing a forward price mechanism at the very point where it is probably weakest.

When shifts in production are needed quickly, price inducements are frequently not sufficient because many farmers are slow to adjust their production plans, even when prices are adequate. An agency like the AAA might by carefully planned payments induce farmers to change their production practices more quickly and to go further than they would when guided by prices alone.

Educational programs may also facilitate the operation of a system of forward prices. This would be especially true of information in the field of farm management which would point out to farmers the advantages of new production techniques and the best organization of the enterprises of the farm. It is quite possible that under most circumstances a well-developed educational program would suffice; that is, it would not be necessary to have additional monetary induce-

ments for desirable farm practices, such as the AAA might facilitate with its personnel and funds.

The Farm Security Administration also seeks to facilitate better use of resources on the part of low-income farm families and in this sphere has an important role to play. There is much capital rationing in agriculture on farms producing less than \$1,000 income annually. On many of these farms additional capital will earn returns much greater than is usually expected at the margin. For example, when the going rate of interest may be 7 percent, additional capital is employed in most business enterprises until it will not earn more than that. What capital rationing implies is that there are many farms on which additional capital would earn not 7 percent but 10, 15, 20, and even larger amounts. To the extent that the FSA is successful in correcting this feature, it will contribute to a solution of both the production and income problems in agriculture.

Six. POSITIVE PROPOSALS: ON THE INCOME SIDE

The welfare branch of economics has not had the sunshine and growth which the monetary, fiscal, and production branches have enjoyed. It is not as stout and strong, and it will not carry as heavy a load. Thus our positive proposals on the income side are more restricted than those for production. Before entering into them, however, it will be helpful to bring together the gist of the preceding discussions on income.

- One.* As in production, there also is a drift toward more national housekeeping on the income side. Public agencies are concerned not only with the size of farm income but also with its distribution and the use to which it is put.
- Two.* Society has a basic interest in farm incomes. This interest is best served when incomes are distributed and used in such a way as to maximize social benefits. The governing criteria are found in social welfare.
- Three.* The incomes farm families receive for their work and the use of their property are often inadequate to support the farm families. It therefore becomes

necessary to supplement the incomes of some farm families.

Four. The price mechanism of farm products is not an appropriate means for supplementing the incomes of farm families. To manipulate farm prices in order to attain certain income goals leads to waste and losses on the production side. This means that tying farm prices to income parity is not an appropriate solution for low farm family incomes, nor does a better allocation of farm resources always improve the distribution of farm family incomes.

Five. The task of improving the income of farm families must be approached as a separate and additional problem to that of managing production. The ways and means of accomplishing this task must be designed specifically for the purpose of supplementing incomes.

This summary does not point to any specific proposals. Instead it simply starts us on the right fork of the road.

FOUR RULES

What, then, can be done to supplement farm incomes in accordance with social welfare criteria? There are some rules to guide us in this. The first is negative in its implications. It may be formulated thus: grants in aids to farm families which are allocated according to production criteria are likely to be ineffective in supplementing farm family incomes. For instance, benefit payments of the AAA type, when allotted according to the size of a farm, the productivity of a farm, the acreage of key crops—such as cotton, corn, wheat, tobacco, or rice—or some other criteria associated with the production side of a farm, enhance the returns of those farm families who already have adequate

incomes much more than they do of those families whose incomes are deemed to be too small from a social welfare point of view.

Iowa data for 1939-1940 obtained by Dr. L. W. Witt show how AAA payments pyramid on farms with the highest incomes.

*Farms classed according
to net income*

Cash from AAA

Upper third	\$350
Middle third	179
Lower third	152

Dr. Witt's figures understate the spread, since benefit payments to landlords are not included. Moreover, the range in size of farms and in incomes is fairly narrow in Iowa compared to many other farming areas, especially in the South.

Most of the government payments going to farmers in recent years have been distributed by AAA. The annual amount has fluctuated around a half billion dollars which in 1939 accounted for 9.5 percent of the total farm income. These government payments have been exceedingly regressive in their effect on farm incomes, meaning simply that the farm families needing additional income most urgently have been granted the least, while those needing it least have received the largest payments.

The second rule in supplementing incomes, whether farm or non-farm, is as follows: The nation expects certain performances in the use of the additional income, performances which will serve the general interest. It is not likely that the government will take a part of the social product and give it to low-income families to do with as they may choose. Society requires that this supplementary income be used to do those things which if left undone would weaken the indi-

vidual members of a family and thereby society. What a nation is interested in is the number and quality of the population; the food, housing, and shelter as these contribute to health and to social outlook; the medical attention people receive; and the education to which they submit themselves. The area of agreement regarding the nature and importance of each of these is steadily increasing. The nation wants all people to have a larger measure of these benefits. Thus we are prone to make them available to all as public benefits, with the proviso, however, that they must be used for specified purposes and not be diverted to "private" uses. This rule suggests that supplementary income is most appropriately granted in kind; in the form of specific public services such as food, houses, medical services, education, etc., and not in the form of a check as are benefit payments. A check once received is cashed and may be used for any purpose whatsoever. It may be used to drive up the price of land and thus squeeze out of farming those who receive the smallest payments.

A third rule which is less general in its scope is as follows. It usually is best to make the supplementary income available on equal terms to all families regardless of their income status. Social benefits of this type have a high rating because they preserve certain democratic values. They avoid the stigma of poor relief; they do not separate people into those who pride themselves in self-support and those who are looked down upon as indigent. Instead, this procedure has the effect of cementing together segments of the population. Elementary education has been financed in this way in most of the United States. The rural free delivery of mail and parcel post is another example. Distributing public services in this way frequently gives the greatest help to low-income families, as is true of the distribution of free milk for all children at school.

The fourth rule is essentially the converse of the first, which was put in a negative form; that is, supplementary income should be tied to the farm family, the home, to consumption, which in the last analysis means relating it to the human agent. This is in contrast to supplementing income on the basis of property resources—such as farm land, the size of the farm, etc.—or tying it to the farm as a business concern. By focusing upon the family and its consumption, the emphasis falls upon the use to which the income is put, and it is at this point where one can determine whether or not the performance is in line with social welfare criteria. Consumption here is broadly defined to include those elements which contribute to higher political and social, as well as to economic, efficiency, and therefore includes not only the elementary physical requirements of food, clothing, and shelter which make for essential bodily well-being but also those things which people do that contribute positively to their social outlook and values as responsible citizens in a democracy.

FAMILY AND NATION

A population policy is probably the key for unlocking the low-income problem.

The change in birth rates and its effect upon the number and composition of the population in the United States are similar to those of western Europe. Some countries, especially Sweden, have become quite aware of the implications of these changes in population and are taking positive steps to remedy them. There is less awareness of the elements of the population problem in this country, although there are some signs that, had the war not come, we soon would have awakened.

Thus, public opinion has not as yet forged the design of a population policy.

Even a cursory knowledge of social processes suggests that agriculture and especially the low-income families in agriculture, will have to receive major attention in any population policy that this nation formulates. The birth rate in agriculture is high relative to other occupations. It still is much higher than is necessary to replace farm people. Thus, there has been—as has been true from the beginning—a marked surplus of children, making it necessary for many farm people to migrate to other locations and to enter other lines of work. The cost of rearing children falls primarily upon the local community and upon the family itself. The community, namely, the school district as education is financed in the United States, bears the brunt of the cost. Rural areas with a high ratio of farm people to resources and a high birth rate find the burden of educating their children much heavier than do those communities in which both resources and incomes per family are much larger and the birth rate much lower. These facts are all well known.

Families with low incomes are bearing a wholly disproportionate share of the cost of rearing the nation's children. This cost is in terms of food, clothing, shelter, medical service, and education. These costs not only place a severe strain upon the budget but often exceed the ability of the family to provide for the children the minimum essentials. As a result, many children on farms and in non-farm communities are not privileged to eat enough nutritious foods, obtain the needed medical attention, or attend school (often taught by poor teachers) more than a few months during the year.

This question constantly arises: How much should be invested in the human agent and who should bear the cost? When we realize that many people migrate from the community in which they are reared to another community, it is clear that both communities are affected. The community that receives is interested in the quality of the human agent,

preferring to add to its numbers individuals who are of good health, who have had at least a minimum education, and who have a social outlook consistent with democratic values. The community from which a person has migrated loses the investment it has made in the human agent, and the greater the investment the larger the loss.

It means, in substance, that the persons who migrate, each of whom has been a cost to the farm family and to the community in which he was reared, put in their appearance as a valuable resource free of charge in another community which has borne none of the cost of rearing them. This is not very different in principle than, for example, if one community were to manufacture a car that cost \$1,000 or more and then sent it to another community as a free gift.

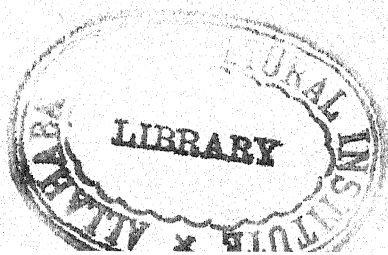
As farm people become aware of the cost of rearing children, as the economic contributions of farm children become less with increasing demands on their time to attend school, and as these families know of and are willing to practice voluntary parenthood, they, too, tend to rear smaller families, partly in order to "compete" on more even terms with other families who do not rear as large a number of children. Granted that the problem has a much larger social matrix and that it cannot be resolved in economic terms, nevertheless, it is, in part at least, related to cost and incomes along the lines just indicated.

The nation has a vital interest in correcting this situation. The number and the quality of the people are at stake. Changing the downward drift in the birth rate and improving the quality of populations involve supplementing the incomes of those families whose incomes are inadequate. The size of the family may well be a major determining factor in the amount of supplementary income that is made available. For example, benefit payments based on the size of the family would make considerable sense, especially if

the payments were granted in the form of such specific services as would assure society that the benefits would be used in rearing children better than would otherwise be the case and would not be diverted to other uses.

In our positive proposals on the income side we have not featured administrative machinery. Instead, we have outlined general rules of procedure and have stressed the importance of population policy.

Prices have a role to play, however. One of the functions of prices is to allocate goods and services to consumers. This part of the price mechanism may be separated from that part that guides and directs production. Thus, prices are also a means for managing consumption and can be used to supplement the incomes of families. In the main, however, this approach has more to contribute to the solving of low-income problems in urban society than among farm people. The role of prices on the consumption side, especially as a means for managing the distribution of the food supply, is another policy field and deserves separate treatment.



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